

## **ABSTRACT**

*In this paper I measure and analyse public sector performance and efficiency for 38 local government in Jawa Timur in 2004-2005 associated with the implementation of fiscal decentralization in Indonesia.*

*The main effect of fiscal decentralization is to provide improved resource allocation and therefore improved economic efficiency. Improved efficiency is the main effect expected from fiscal decentralization. Efficiency gains rest on the presumption that local government are much better in identifying and fulfilling the needs of households, since they are closer to them, and in mobilizing and using local resource to pay for goods and services having purely local impacts. Once improved efficiency could be gained, public sector performance increase.*

*I compute public sector performance (PSP) and efficiency (PSE) indicators comprising a composite consists of six sub-indicators. The first three indicators reflects socio-economic indicators that take into account administrative, education and health outcomes. Three other indicators reflect the standard “musgravian” task for government : distribution, allocation and stabilization. Then, the model is applied to measure public sector performance and efficiency of the local government in Jawa Timur.*

*I use Free Disposable Hull (FDH), a non-parametric framework, to compute a so-called production possibility frontier and calculate input efficiency and output efficiency scores in order to rank the local government in terms of public spending efficiency. The results of the FDH calculations show that the average local government output efficiency score in 2005 is lower than that in 2004. The decreased of efficiency indicates problems or something wrong with the implementation of fiscal decentralization.*

*Finally, in order to see what non-discretionary factors may impinge on the efficiency level of local government services provision, I performed a Tobit Periode Fixed Effect Panel Data Analysis. The Tobit analysis suggests that Human Development Index which is used as a proxy for measuring the level of people empowering has significantly and positively effect to public sectors efficiency. On the other hand, the local governments with receiving higher grants from central government are the most inefficient in the management of their resource.*

*Based on the evidence found from Tobit Analysis, improved public sector performance and efficiency of the local government in Jawa Timur depend on the qualitative measurements or non-monetary indicators, like Human Development Index.*

**Keywords :** *Fiscal Decentralization, Public Sector Efficiency (PSE), Public Sector Performance, Free Disposable Hull (FDH), Tobit.*